

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

JOHN R. OLSON and SOLVEIG L. OLSON,
Derivatively on Behalf of Nominal Defendant
KANDI TECHNOLOGIES GROUP, INC.,

Plaintiffs,

v.

HU XIAOMING, BING MEI, CHEN LIMING,
JERRY LEWIN, HENRY YU, CHENG WANG,
XIAOYING ZHU and YI LIN,

Defendants,

and

KANDI TECHNOLOGIES GROUP, INC.,

Nominal Defendant.

Civil Action No:

JURY TRIAL DEMANDED

VERIFIED SHAREHOLDER DERIVATIVE COMPLAINT

Plaintiffs John R. Olson and Solveig L. Olson (“Plaintiffs”), by their undersigned attorneys, submit this Verified Shareholder Derivative Complaint against the Defendants (defined below) named herein, and allege upon personal knowledge with respect to themselves, and upon information and belief based upon, *inter alia*, a review of public filings, including: (i) filings with the United States Securities and Exchange Commission (“SEC”); (ii) press releases and reports issued by Kandi Technologies Group, Inc. (“Kandi” or the “Company”); (iii) pleadings and other filings in the securities fraud class action lawsuits captioned *Nunziatina Paolini v. Kandi Technologies Group, Inc. et al.*, 2:17-cv-2025 (C.D.Cal.), *Cashen v. Kandi Technologies Group, Inc. et al.*, 1:17-cv-1944 (S.D.N.Y.); *Reichenstein v. Kandi Technologies Group, Inc. et al.*, 1:17-cv-1930 (S.D.N.Y.) and *Tavrovsky v. Kandi Technologies Group, Inc., et al.*, 1:17-cv-03049

(S.D.N.Y.) (collectively, the “Securities Class Actions”); and as to all other allegations herein (iv) an investigation undertaken by Plaintiffs’ counsel as follows:

NATURE OF THE ACTION

1. Plaintiffs bring this action derivatively for the benefit of Nominal Defendant Kandi against certain of the Company’s current and former executive officers and directors seeking to remedy the Defendants’ breaches of fiduciary duties and violations of the Securities Exchange Act of 1934 (the “Exchange Act”) for issuing false and misleading statements and/or omitting material information in the Company’s public filings from May 12, 2014 to the present (the “Relevant Period”).¹

2. The Company develops, manufactures and commercializes electric vehicles (“EVs”), all-terrain vehicles, battery packs, automobile motors, controllers for EVs, and air-conditioning systems.

3. In 2013, the Company partnered with Geely Automobile Holdings Ltd. (“Geely”) in a 50/50 joint venture (the “Joint Venture” or the “JV Company”) to manufacture EVs. The Company entered into the Joint Venture in order to take advantage of lucrative subsidies for manufacturers and purchasers of EVs given out by China’s central and provincial governments at the time. As a result, since entering into the Joint Venture, the Company has derived almost all of its revenues from its stake in the Joint Venture. However, Kandi – along with several other EV manufacturers – has been “double dipping” in the two subsidies that has since caused China to reduce the subsidy program with a mandate to eventually do away with it altogether.

¹ The materially misleading statements and/or omissions were issued in the Company’s financial reports and other public filings and releases from approximately May 12, 2014 to March 13, 2017; however, the wrongs complained of herein continue through to the present as the Company’s internal controls remain deficient.

4. Prior to early 2016 when Chinese officials first started learning about the subsidy scheme being perpetrated by several companies, including Kandi, the Company's business model was generally as follows: Kandi would sell auto parts to the Joint Venture (in which it has a 50% stake and Geely had, until recently, the other 50% stake). The Joint Venture would produce the EVs and then sell them to a Chinese entity called Zuozhongyou ("ZZY"), which purportedly used the EVs in a car share operation, as a purchaser. This arrangement was rife with conflicts orchestrated by Kandi's management as ZZY is 9.5% owned by Kandi and another 13% of ZZY is owned by Kandi's Chairman, defendant Xiaoming.

5. Through this arrangement, Kandi was able to take advantage of both subsidies offered by China's central and provincial governments since one subsidy was given out to manufacturers of EVs and the other was given out to purchasers of EVs. Thus, the Joint Venture, as a manufacturer, was eligible for the first subsidy and ZZY was created in an effort to take advantage of the second subsidy for EVs as a purchaser from the Joint Venture.

6. This way, Kandi only had to manufacture parts for EVs, sell them to the Joint Venture and then "double dip" both subsidies after the Joint Venture manufactured the EVs and later sold them to ZZY. The benefits of both subsidies could be worth more than the cost of building the vehicles.²

7. However, as Kandi and other imitators took advantage of the subsidy scheme and the EV industry achieved extraordinary growth in China, in late 2015 and early 2016, news of the scandal emerged as government regulatory, industry experts and investigative journalists started

² See SerrCo, *Kandi Technologies: Chinese EV Clunker Begins To Break Down Amid Subsidy Scandal, 70% Downside*, SeekingAlpha (Aug. 18, 2016), available at <https://seekingalpha.com/article/4000616-kandi-technologies-chinese-ev-clunker-begins-break-amid-subsidy-scandal-70-percent-downside>.

paying attention.

8. As one of the innovators of the subsidy scheme, Kandi was at the center of the investigation when *Caixin*, one of China's biggest financial journals, published a story on Kandi and China's EV subsidy fraud problem. *See supra* note 2.

9. Since the news of the subsidy fraud began to emerge and Chinese regulatory agencies began investigating EV producers such as Kandi, the Company's sales began to plummet.

10. In the wake of the subsidy fraud being exposed, throughout the Relevant Period, Defendants caused the Company to issue false and misleading statements and/or omit material information concerning the Company's business, operations, prospects and/or compliance policies. In particular, the Company issued false and misleading statements and/or failed to disclose, *inter alia*, that: (i) Kandi's previously issued financial statements for the years ended December 31, 2015 and 2014 and the first three quarters for the year ended December 31, 2016, contained numerous sections that the Company was required to adjust; (ii) the Company lacked adequate and effective internal controls over financial reporting; and (iii) as a result, the Company's public statements issued throughout the Relevant Period were materially false and misleading.

11. Since the truth about the Chinese EV producer industry began to emerge, the Company reported that the Joint Venture's sales came to a halt in the first quarter of 2016 as Kandi disclosed that zero EVs were sold in that quarter. The Joint Venture also reported a negative \$500,000 in revenue in the first quarter of 2016 and Kandi disclosed it had yet to receive any subsidies for the EV sales that occurred in 2015.

12. Chinese regulators acted quickly to reduce available subsidy payments by mandating that the subsidies be phased out over the next four years, with full elimination of the

subsidy payments thereafter.

13. According to the article by *SeekingAlpha* (*supra* note 2), a few weeks after the news about the subsidy program being eliminated emerged, Kandi's auditor, Albert Wong & Co., was banned from the auditing industry for failing to investigate obvious signs of fraud by Kandi's management, including an instance where defendant Xiaoming and another Kandi financial controller produced personal bank account statements as evidence of the Company's cash on hand.

14. Further, on July 25, 2016, Geely announced that it was selling its stake in the Joint Venture at a valuation barely above book value.

15. On March 13, 2017, the Company filed a current report on Form 8-K with the SEC which stated, in pertinent part:

Item 4.02 Non-Reliance on Previously Issued Financial Statements or a Related Audit Report or Completed Interim Review.

...the Company's management identified certain areas in the Company's previously issued financial statements for the years ended December 31, 2015 and 2014, and the first three quarters for the year ended December 31, 2016 (the "Previously Issued Financial Statements"), that require adjustment...

The Restatements will include separate audited financial statements for the Company's equity investment in the JV Company, corrections to the classification of notes receivable and notes payable in the Company's statements of cash flow, revisions in the Company's financial statement presentation to separately identify certain related party accounts on the face of the Balance Sheets and the Consolidated Statements of Income (Loss) and Comprehensive Income (Loss), certain amendments to Note 20 – Taxes of the Notes to the Company's Consolidated Financial Statements, the adjustment of previously recorded construction-in-progress back to prepayment in Note 16 - Construction-in-Progress of the Notes to the Company's Consolidated Financial Statements, expansions of two tables of sales to and purchases from the JV Company in Note 24 – Summarized Information of Investment in the JV Company of the Notes to the Company's Consolidated Financial Statements from two years to three years, and the removal of "unaudited" labels from certain tables in Note 20 - Taxes of the Notes to the Company's Consolidated Financial Statements.

The Company will also amend its unaudited quarterly data for the first three quarters ended December 31, 2016, as set forth in its upcoming Annual Report

*on Form 10-K for the year ended December 31, 2016.*³

16. On this news, the Company's stock dropped from a close of \$4.35 per share on March 13, 2017 to close at \$4.05 per share on March 14, 2017, a loss of \$0.30, or approximately 6%, on unusually heavy volume of approximately 513,200 shares.

17. In furtherance of the wrongdoing described herein and while the truth concerning Kandi's business and prospects had yet to be revealed, the Company's management awarded themselves excessive compensation throughout the Relevant Period. In particular, for the fiscal year ended December 31, 2015, stock-based compensation for Kandi's management was \$22,306,987. Form 10-K, at F-7, filed with the SEC on March 14, 2016 (the "2015 10-K"). The over \$22 million in stock-based compensation awarded to the Company's management in 2015 accounted for 78% of gross profits and more than 68% of the Company's operating expense. If that was not enough, in the first half of fiscal year 2016, stock-based compensation rose to \$15,134,658, an increase of over 200% from the same period in the prior year. Form 10-Q, at 4, filed with the SEC on August 9, 2016 (the "Q2 2016 10-Q").

18. Kandi and its shareholders have been harmed and continue to suffer from Defendants' wrongful conduct described herein.

JURISDICTION AND VENUE

19. This Court has subject matter jurisdiction pursuant to §27 of the Exchange Act, 15 U.S.C. § 78aa, as well as 28 U.S.C. § 1331. This Court has supplemental jurisdiction over the state law claims pursuant to 28 U.S.C. § 1367(a). In connection with the acts, conduct and other wrongs complained of herein, Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, the United States mail and the facilities of a national securities market. This

³ All emphasis added unless otherwise noted.